Pensions Update

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BAKER & McKENZIE

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Brexit: pension implications

On 23 June 2016, the British public voted in a referendum in favour of "Brexit", or exit from the European Union ("**EU**").

Implications for pensions law: much of UK pensions law which is derived from EU law is contained in primary legislation, including, for example, the scheme specific funding requirements for DB schemes. We think that it is unlikely that there will be significant change to this existing body of law as a result of the vote to leave. It is possible that we may see some future divergence in some areas depending on how law develops in the EU and that nature of the UK's relationship with remaining EU27 which emerges over the following months and years.

Impact on key funding risks for DB schemes: Trustees and sponsoring employers of occupational DB pension schemes will need to factor in the impact which the leave vote will have on key funding risks in the scheme: covenant, investment risk and how the funding level and strategy for the scheme is set. Again, much is likely to depend on the nature of the revised UK/EU-27 relationship and the particular industry in which the sponsoring employer operates.

For sponsoring employers, maintaining ongoing dialogue and communications with trustees will be key. In the event of the vote to leave having a significant adverse impact on the business, for example a reduction in credit rating, employers should consider whether any legal requirements to communicate information to trustees are triggered. For example, this could be the case under a parent company guarantee or any information sharing agreement which is in place between the employer and trustees. There is also a legal requirement on employers to disclose to trustees "*any event relating to the employer which there is reasonable cause to believe will be of material significance in the exercise by the trustees…..of any of their functions.*"

For Trustees, although Brexit represents uncharted territory, its potential impact needs to be carefully considered like any other significant development that may affect the scheme. In the weeks and months ahead, Trustees will, no doubt, continue to ensure an appropriate dialogue with the employers and make use of their existing monitoring and governance procedures.

We will be considering what the Brexit vote means for pensions in more detail at our breakfast briefing on 13th July. If you would like to come along and have not yet registered to attend, you can register here.

BREXIT: Keep up to date on the latest Brexit developments – follow the Baker & McKenzie Brexit Blog

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VAT input tax recovery by the taxpayer where services are provided to others

By a majority of 3-2, the UK Supreme Court has held that a taxpayer cannot recover input tax where it pays for services supplied to another party if the service provider is not obliged to perform those services.

In 2002 Airtours (the taxpayer) was in serious financial difficulties. It wished to refinance its debts in order to restructure its business. The lenders agreed to it commissioning a report on its restructuring proposals, and they and Airtours decided to appoint PwC to produce a report.

Airtours sought to deduct as input tax the VAT it paid on PwC's fees. HMRC objected, arguing that PwC's services were not supplied to Airtours under the contract, and Airtours was therefore not entitled to the deduction.

Essentially, the Supreme Court had to decide whether PwC had contracted to supply services to Airtours. The majority found that, in this particular case, PwC's contractual commitment was to the lenders, not to Airtours.

The decision will be of interest to employers with occupational DB schemes, who have been grappling with the issue of how to maximise the recovery of VAT on services which are supplied in relation to a pension scheme.

There have been a number of developments in this area, including in HMRC's approach, which we have reported on in previous updates (**December 2014 update**, **April 2015 update** and **October 2015 update**). In the context of this decision, the most relevant change in HMRC's approach is the requirement that, from 1 January 2017, the employer (taxpayer) must be able to provide that it had actually received the services, including the employer being a party to the contract with the suppler, paying for the supply and receiving a valid VAT invoice..

The judgment can be accessed here.

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First-Tier Tribunal refuses VAT repayment appeal

The First-Tier Tribunal Tax Chamber in Scotland, in *First State Investment Management (UK) Ltd v Commissioners for HMRC, refused FSIM's* application to have its appeal against HMRC's decision to reject a claim for repayment of £5 million of VAT charged on supplies of investment management services provided by FSIM to defined benefit pension funds stayed due to forthcoming cases, which it argued were "*substantially similar*".

The First-Tier Tribunal rejected the application noting, amongst its reasons, that the other cases were being heard in England and that there would therefore be jurisdictional differences. Additionally, the Tribunal noted that one of the cases on which FSIM wishes to wait (*United Biscuits (Pension Trustees) Ltd and Another v Commissioners for HMRC) has numerous complex issues and is dependent on another case (Investment Trust Companies (in liquidation) v HMRC)* which is to be heard before the Supreme Court and therefore delays will not be avoided by waiting for this decision.

FSIM have been given leave to appeal the decision. We will be providing further updates on these VAT cases as they progress.

The judgment can be accessed here.

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The Pensions Regulator publishes annual funding statement and analysis

The Pensions Regulator has published its annual funding statement alongside its review of defined benefit pension schemes with valuation dates between September 2015 and September 2016.

In the funding statement, the Regulator identifies the key funding issues for schemes carrying out their 2016 valuations, which includes volatility, investment returns, affordability, managing deficits and risks. The statement also details recent developments in valuation assumptions. The statement notes, for example, that the Continuous Morality Investigation model 2015 (CMI2015) provides lower life expectancies than the 2014 version. The Regulator comments that trustees who use CMI can update to CMI2015, but notes that this decision should be considered carefully with advisers.

The Regulator records that its findings for schemes carrying out valuations in 2016 displays that the major asset classes have performed well, although for most schemes the value of their liabilities have increased faster than their assets. Deficits have also increased in the region of 20-35% and the Regulator has modelled the potential impact of these higher deficits on schemes' recovery plans.

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High Court permits rectification by summary judgment without a hearing

In the recent case *of The Girls' Day School Trust v GDST Pension Trustees Ltd & Anor,* the High Court granted an application for rectification by summary judgement following the execution of the incorrect version of a trust deed.

A new definitive deed and rules was drafted to establish a new pension scheme for the GDST. Before finalising the trust deed a number of versions had been created, Versions 1, 1A, 1B and 2. Version 2 contained all of the parties' agreed amendments and should have been the version executed. However, the engrossment prepared for execution and signed was Version 1A.

In permitting rectification by summary judgment without a hearing, Norris J noted that it was "*plain*" that the execution of the earlier version of the trust deed was a *"mistake"* and it was "*equally plain"* what had been intended.

By allowing rectification without a hearing and to dispel the notion of "*a deal done behind closed doors*" he identified the need for adequate publicity of the decision. To achieve this Norris J published the judgment on BAILLI and ordered that the rectification was not to take effect for 42 days after the date of the judgement. All scheme members were to be informed and offered a hard copy of the judgment.

Norris J also tackled the issue of confidential evidence when permitting a summary judgment. He noted that in this case Counsel's opinion was allowed to remain confidential, but this was only because "*full*" evidence was available which had been "*scrutinised and tested*" and because the Opinion had not been prepared in the light of a public disclosure. However, in future rectification cases, Norris J stated that it was likely that the Court "*will insist that after judgment all evidence be open to inspection"* and if this is not acceptable, then a public hearing will be required.

The judgment can be viewed by clicking here.

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Consultation on extending Fair Deal and Local Government Pension Scheme Regulations

The Department for Communities and Local Government has published a consultation to extend Fair Deal to include local authority outsourcings and to consult on the Local Government Pension Scheme (Amendment) Regulations 2016 which will amend the Local Government Pension Scheme Regulations 2013 and the Local Government Pension Scheme (Transitional Provisions, Savings and Amendment) Regulations 2014 to provide clarity and to improve their operation.

The consultation closes on 20 August and can be accessed here.

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Ombudsman publishes new approach to decision publication

The Pensions Ombudsman Service has set out its new approach to publishing decisions on its website.

The Pensions Ombudsman Service website will now publish opinions issued by adjudicators if they are appealed or considered to be of interest. The

Pensions Ombudsman Service has also clarified how published decisions will be anonymised. The name of the member together with any identifying personal data will be removed, unless this information is needed to understand the decision. In certain cases anonymity may be deemed inappropriate for example where the identity of the complainant is relevant to the issue or the case is particularly notable with wider public interest implications. The Ombudsman will communicate with all parties involved should it wish to waive anonymity, but this will ultimately be determined by the Ombudsman on a case by case basis.

To read the statement, please click here.

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Consultation on capping early exit charges for members of occupational pension schemes

The Department of Work and Pensions has launched a consultation on the potential implementation of a cap on early exit charges imposed when a member wishes to exit an occupational pension scheme early to access their pensions flexibly. The Government's consultation in 2015 found that exit charges were being implemented and were *"presenting significant barriers to those who incurred them, potentially prohibiting individuals from accessing their pension benefits flexibly".* Baroness Altman notes that the intention is to remove the *financial barrier* created by early exit charges. The DWP has issued additional analysis on the expected impact of a 1% cap on early exit charges.

The Financial Conduct Authority is concurrently considering the cap to be implemented by personal pension schemes (please see article below for more information) and Baroness Altman notes that the Government will work with the FCA and the Pensions Regulator "*to ensure that all consumers can benefit from the cap, regardless of the pension scheme they have saved into".*

To access the consultation and additional analysis please click here.

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FCA consultation on capping early exit charges

As noted above, the Financial Conduct Authority is also currently considering proposals to cap early exit charges for personal pension schemes to remove barriers to members exercising the new pension freedoms. The FCA has published a consultation on its proposals for the application and level of a cap in response to the Government's introduction of new legislation which places a duty on the FCA to cap early exit charges in personal pension and stakeholder schemes.

The consultation closes on 18 August and the consultation paper can be accessed here.

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